In the Supreme Court of the United States

October Term, 1939

No.................

Herbert Fleishhacker,
Petitioner,
vs.

Lucien Blum, Edmond Lang, Elizabeth Lang, Rene Fould, Esther Fould, Max Lazard, Roger Haas, Andre Haas, Lucie Emile Lewylier, S. A. Johanesson, G. O. Hoffman and Henry Leon,
Respondents.

Brief In Support of Petition for Writ of Certiorari.

POINT I

PLAINTIFFS FAILED TO COMPLY WITH EQUITY RULE 27; AND THE COURT BELOW, BY CONDONING PLAINTIFFS' FAILURE, EMASCULATES THE RULE.

If the decision in the court below concerning the requirements of Equity Rule 27 (now Rule 23(b), Federal Rules of Civil Procedure) is allowed to stand,

then the diversity jurisdiction of the federal courts is open to any stockholder who seeks to have his judgment on questions of managerial policy substituted for that of the Board of Directors, enabling him to compel litigation of the corporation's claims, real or false, even though the Directors decide, for the best of reasons and without breach of trust, it should not be done, and even though all of the other stockholders are in agreement with the Board.

The dissenting opinion of Circuit Judge Mathews in the court below is a clear demonstration of the fact that plaintiffs failed to comply with Equity Rule 27; and that the majority of the court below, by condoning plaintiffs' failure, emasculate both the rule and the substantive principles which it embodies.

Plaintiffs alleged a demand on the Board of Directors to bring this action, and the Board's failure to do so.

But the rule also requires that the Bill:[1]

> "Must also set forth with particularity the efforts of the plaintiff to secure such action as he desires on the part of the managing directors or trustees, and, if necessary, of the shareholders, and the causes of his failure to obtain such action, * * *."

Plaintiffs' only attempt to meet this requirement consists of the following allegation:

(1) Federal Rules of Civil Procedure, Rule 23(b), is substantially identical.

> "Plaintiffs are informed and believe and so allege that the causes for such failure of the Board of Directors to institute an action to recover these profits are that the Board of Directors is composed of relatives, close friends and business associates of the defendant Fleishhacker and are under the domination of the defendant Fleishhacker." (R 17)

But as stated in the dissenting opinion below:

> "This allegation was denied and not proved. * * * There is no evidence that any member of the Board was dominated by Fleishhacker. Only one relative of Fleishhacker was shown to be a member of the Board." (R 922)[1]

The following quotation from the dissenting opinion of Circuit Judge Mathews sums up, we submit, the conclusion to be drawn from the foregoing:

> "The board may, in good faith, have believed that the charges made in the letter were false and unfounded; that Anglo had, in fact, no right of action against Fleishhacker, Klinker, Thompson or Stock Farms; and that it could not, in equity or good conscience, bring suit against them, or leave appellees' suit undefended. Lacking proof to the contrary, we should—and I do—presume that the board acted in good faith. Corbus v. Alaska Treadwell Gold Mining Co., 187 U. S. 455, 463.

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(1) The Bank had a board of 19 members at the time of the transactions in 1919. (R 599) There is no other evidence as to the personnel of the board, their number or identity or relationships, at the time of the demand.

"Even if the board had believed that Anglo had a right of action, it might, also, in good faith, have believed that it was not to Anglo's best interest to bring suit thereon and, so believing, might properly have waived such right of action. Hawes v. Oakland, supra, 104 U. S. p. 462; Corbus v. Alaska Treadwell Gold Mining Co., supra; United Copper Securities Co. v. Amalgamated Copper Co., 244 U. S. 261, 263, 264.

"Having failed to show that the board's failure to sue constituted a fraud or breach of trust, or that it was in any respect wrongful or improper, appellees had, and have, no standing to maintain this suit.

"The decree should be reversed and the case should be remanded with directions to dismiss the bill of complaint." (R 923)

The Decision is Directly Contrary to the Decisions of This Court and of Courts Generally Including California.

This Court has laid down the rule that the power and duty of management of a corporation is vested in the board of directors; and absent fraud, bad faith or illegality, the courts will not permit (much less enable) a stockholder to insist that his judgment, rather than the board's, shall dictate the corporation's course of action.

The leading case is *Hawes v. Oakland,* 104 U. S. 450.

The authorities in general are collected in

13 Fletcher, *Cyc. of Corporations* (Perm. Ed.) Secs. 5969, 5822.

As stated by Mr. Justice Brandeis in *Ashwander v. Tennessee Valley Authority,* 297 U. S. 288, 343, in his concurring opinion joined in by Mr. Justice Stone, Mr. Justice Roberts and Mr. Justice Cardozo:

> "Within recognized limits, stockholders may invoke the judicial remedy to enjoin acts of the management which threaten their property interest. But they cannot secure the aid of a court to correct what appear to them to be mistakes of judgment on the part of the officers. Courts may not interfere with the management of the corporation, unless there is bad faith, disregard of the relative rights of its members, or other action seriously threatening their property rights. This rule applies whether the mistake is due to error of fact or of law, or merely to bad business judgment. It applies, among other things, where the mistake alleged is the refusal to assert a seemingly clear cause of action, or the compromise of it. United Copper Securities Co. v. Amalgamated Copper Co., 244 U. S. 261, 263-264. If a stockholder could compel the officers to enforce every legal right, courts, instead of chosen officers, would be the arbiters of the corporation's fate."

The case of *Corbus v. Alaska Treadwell Gold Mining Co.,* 187 U. S. 455, was, as here, a stockholder's suit by the holder of a very small proportion of stock. This Court pointed out the small interest of plaintiff, noted also that the other stockholders had not shown any interest in the alleged wrong, and spoke as fol-

lows (p. 463), concerning Equity Rule 94, the predecessor of Equity Rule 27 and the present Rule 23(b):

> "It must not be understood that a mere technical compliance with the foregoing rule is sufficient and precludes all inquiry as to the right of the stockholder to maintain a bill against the corporation. This court will examine the bill in its entirety and determine whether, under all the circumstances, the plaintiff has made such a showing of wrong on the part of the corporation or its officers and injury to himself as will justify the suit. The directors represent all the stockholders and are presumed to act honestly and according to their best judgment for the interests of all. Their judgment as to any matter lawfully confided to their discretion may not lightly be challenged by any stockholder or at his instance submitted for review to a court of equity. The directors may sometimes properly waive a legal right vested in the corporation in the belief that its best interests will be promoted by not insisting on such right. They may regard the expense of enforcing the right or the furtherance of the general business of the corporation in determining whether to waive or insist upon the right. And a court of equity may not be called upon at the appeal of any single stockholder to compel the directors or the corporation to enforce every right which it may possess, irrespective of other considerations. It is not a trifling thing for a stockholder to attempt to coerce the directors of a corporation to an act which their judgment does not approve, or to substitute his judgment for theirs."

And this Court said in

United Copper Securities Co. v. Amalgamated Copper Co., 244 U. S. 261, at 263-4:

"Whether or not a corporation shall seek to enforce in the courts a cause of action for damages is, like other business questions, ordinarily a matter of internal management and is left to the discretion of the directors, in the absence of instruction by vote of the stockholders. Courts interfere seldom to control such discretion *intra vires* the corporation, except where the directors are guilty of misconduct equivalent to a breach of trust, or where they stand in a dual relation which prevents an unprejudiced exercise of judgment; and, as a rule, only after application to the stockholders, unless it appears that there was no opportunity for such application, that such application would be futile (as where the wrongdoers control the corporation), or that the delay involved would defeat recovery. In the instant case there is no allegation that the United Copper Company is in the control of the alleged wrongdoers or that its directors stand in any relations to them or that they have been guilty of any misconduct whatsoever. Nor is there even an allegation that their action in refusing to bring such suit is unwise. No application appears to have been made to the stockholders as a body or indeed to any other stockholders individually; nor does it appear that there was no opportunity to make it, and no special facts are shown which render such application unnecessary. For aught that appears, the course pursued by the directors has the approval of all the stockholders except the plaintiffs."

The California rule is the same. Thus in *Waymire v. San Francisco etc. Ry. Co.,* 112 Cal. 646, 649, the Supreme Court of California said:

> "Therefore, as a general rule, the action should have been brought by and in the name of the corporation; but when, upon proper demand by stockholders, the corporation *wrongfully* refuses to institute an appropriate action, or when it appears that such demand by stockholders would have been unavailing and fruitless, an action may be instituted and prosecuted by a stockholder for the direct and immediate benefit of the corporation, and for the incidental benefit of the stockholders."

The italics in the above quotation are the court's. Again, in

> *Thomson v. Mortgage Investment Co.,* 99 Cal. App. 205, 215,

the court said:

> "* * * such actions may be instituted and maintained by stockholders only when the acts of the board of directors of the corporation are either *ultra vires,* illegal, fraudulent, oppressive or show wilful neglect. (Fletcher's Cyclopedia of Law of Private Corporations, sec. 4065; Hawes v. Oakland, 104 U. S. 450. * * *)"

See, also, *Difani v. Riverside County Oil Co.,* 201 Cal. 210, 215 and cases cited; *Whitten v. Dabney,* 171 Cal. 621, 630; *Cogswell v. Bull,* 39 Cal. 320, 324.

But the court below has announced and applied a very different rule; namely, that any stockholder who

chooses to, may demand that the corporation bring an action and, if refused, may, without either pleading or proof that the corporation's refusal to sue was wrongful, maintain the action on its behalf, even though the board of directors believes and decides, and even though it is a fact, that prosecution of the action is unwise or will be unjust, or futile, or harmful to the corporation.

The Opportunities for Misuse of Stockholders' Suits Are Unlimited Under the Rule Announced Below.

Equity's allowance of suits by stockholders is necessary to avoid injustice, but dangerous, because of the misuse of such suits by misguided or meddlesome dissenters, and as indirect means of extortion or coercion. See the many references under Rule 23(b) in Moore's Federal Practice, Vol. 2, pp. 2246-76.

See, also, an excellent note, *"Extortionate Corporate Litigation"*, 34 Columbia Law Review, 1308.

See, also, *"A History of The Libel Suit of Clarence H. Venner against August Belmont"* (1913).

The court below, without adding anything to the value of stockholders' suits, makes them a perfect instrument for the accomplishment, by indirection, of wholly illegitimate ends.

Federal Diversity Jurisdiction Can Be Manufactured Almost at Will Under the Rule Announced Below.

Any dissident stockholder or group who can find a non-resident stockholder willing to act as plaintiff,

can thereby create federal diversity jurisdiction of any suit such as this.

If, as held below, any stockholder may bring suit on any real or pretended cause of action which the corporation refuses (for the best of reasons) to prosecute, then this source of litigation in the federal courts is enormously enlarged.

The rule announced below, therefore, not only destroys the principle that the directors and not individual stockholders should decide questions of management, but makes the federal courts the agency for destroying that principle (since virtually all states hold the contrary), and invites a great and uncontrolled expansion of such misuse of the federal courts. Here both Petitioner and the Bank are citizens of California.

Petitioner Was Not Allowed to Show the Reasons for the Bank's Refusal to Bring This Suit.

The error just discussed is emphasized by the fact that the trial court excluded Petitioner's evidence offered to show why the Board of Directors of the Bank refused to bring this suit. (R 630-32, 786) In the assignment of error on this point the substance of the evidence thus excluded is summarized as follows (R 786, 792-94):

> "The substance of the evidence which defendant would have introduced but for said exclusion by the Court is as follows:

"The Board of Directors had knowledge of the transactions complained of in the Bill of Complaint, and had made an independent investigation of same prior to its receipt of the demand of Etienne Lang; and upon receipt of said demand again investigated and reviewed the same.

"The investigation made by the Board resulted in the ascertainment by it of the following facts:

"a. That the Bank had knowledge of said transactions in December 1919 and January 1920, when said loans were made, and at all subsequent times.

"b. That the Bank had knowledge in December 1919 of the personal interest of defendant Herbert Fleishhacker in the steel venture in which the proceeds of the loans were employed and of his hope to make a personal profit therefrom, which facts were disclosed to it by said defendant.

"c. That the Bank at and from the time of said transactions consented to the participation of defendant Herbert Fleishhacker in the said venture and to the receipt and retention by said defendant of the profit therefrom.

"d. That the Board of Directors had knowledge of all of the facts as to the activities of Lang which were later revealed at the trial.

"e. That the demand was not made in good faith, but was made for the purpose of injuring the Bank, and aiding the members of the Lazard family (represented by Lang) in other litigation in which large sums of money were demanded for alleged frauds by the Bank and its chief executive officer.

> "The Board concluded after such investigation, that the Bank did not have any valid, legal or equitable claim as a result of said transaction, and that the institution of suit thereon would injure the Bank.
>
> "The members of the Board at all said times were independent of defendant Herbert Fleishhacker, and were not dominated or controlled by him and had no adverse interest to the Bank."

The view entertained below is thus made clear: Although a corporation refuses to bring suit in entire good faith, and for the best of reasons, and all but one stockholder agree, nevertheless, that one stockholder may compel complete litigation of the corporation's alleged claim by proceeding in the federal courts, provided only that diversity of citizenship between the complaining stockholder and the real defendant can be shown.

It is unnecessary to labor the point that the trial court's exclusion of Petitioner's evidence offered to show the Board of Directors' investigation of plaintiff's demand to sue, the results of that investigation, and the reasons which impelled the Board (acting without domination or adverse control) to refuse the demand, was prejudicial error. This because, as the authorities abundantly show, the ultimate question as to the right of a stockholder to sue on behalf of a corporation is whether or not the refusal of the corporation itself to sue was wrongful.

Moreover, the decision of the inferior courts excluding as immaterial as a matter of substantive law the reasons why the Board of Directors refused to

bring suit, directly opens the federal courts to collusive suits wherein no true diversity of citizenship exists: this because, if such reasons are immaterial as a matter of substantive law, then whether they be valid or the result of collusion to create a false diversity of citizenship, no inquiry as to those facts may be had.

Plaintiffs' Interest in the Bank Is Slight; No Other Stockholders Complain.

Plaintiffs own in the aggregate 1554 shares of the stock of the Bank out of 770,000 shares outstanding. (R 44-5, 132) Plaintiffs, therefore, own about 2/10ths of 1% of the outstanding stock in the Bank. And they only owned 174 shares at the time (1919) of the acts complained of. Their respective holdings, and their respective monetary interest in the judgment recovered, are as follows (R 44-45, 132):

	Shares	*Date Acquired*(1)	*Interest in recovery.*
Rene Fould and Esther Fould	8	April 1, 1909	$ 7.68
Edmond Lang and Elizabeth Lang	2	April 1, 1909	1.92
S. A. Johanesson	12	October 28, 1918	11.52
Lucien Blum	128	March 25, 1910	122.88
Max Lazard	8	April 1, 1909	7.68
G. O. Hoffman	16	October 28, 1918	15.36
Henry Leon	248	April 7, 1922	238.08
Roger Haas	416	November 27, 1928	399.36
Andre Haas	416	November 27, 1928	399.36
Lucie Emile Lewylier	300	July 12, 1932	288.00

(1) There is absolutely no evidence to support the finding that Henry Leon was a stockholder at all times mentioned in the Bill (R 295) or the finding that the stock of Roger Haas, Andre Haas, and Lucie Emile Lewylier devolved on them by operation of law. (R 312)

The relatively microscopic interest of the plaintiffs in the subject-matter of this suit, and the fact that so far as appears all of the other stockholders in the Bank were and are entirely satisfied with the course taken by the directors are plainly persuasive evidence, (a) that the claim is in fact without foundation, and (b) that the Board of Directors' decision not to sue was a proper exercise of the Board's discretion. The authorities make this clear. See *Corbus v. Alaska, etc. Gold Mining Co.*, 187 U. S. 455, 463; *United Copper Securities Co. v. Amalgamated Copper Co.*, 244 U. S. 261, 263-4; *Carson v. Allegany etc. Co.*, 189 Fed. 791; *Presidio Mining Co. v. Overton*, 261 Fed. 933, 940.

POINT II

THE ACTION IS BARRED BY LACHES AND THE STATUTE OF LIMITATIONS

If a suit brought by the Bank itself would have been barred by laches or the statute of limitations, then, of course, this stockholders' suit, brought on behalf of the Bank, is likewise so barred.

> 13 Fletcher, *Cyc. of Corporations* (Perm ed.) Sec. 5947;
>
> *Earl v. Lofquist*, 135 Cal. App. 373, 376-8.

The Bank is the "aggrieved party" under the California Statute of Limitations. (*People v. Noyo Lumber Co.*, 99 Cal. 456, 461; 16 Cal. Juris. 503-4).

It follows that the plaintiff must show that the corporation's right to sue has not been lost; and in

this behalf must plead and prove facts which excuse the corporation's fifteen-year delay in asserting the cause of action put forward on its behalf.

> 13 Fletcher, *Cyc. of Corporations* (Perm. ed.) Sec. 6005.

Of the almost countless cases laying down the detailed and convincing proof required of plaintiffs seeking to escape from laches or the statute of limitations, in a suit based upon a claim of fraud, where (as here) the events constituting the alleged cause of action took place many years before suit was brought, one of the most important is *Wood v. Carpenter*, 101 U. S. 135. In that case this Court said in part (140):

> "In this class of cases the plaintiff is held to stringent rules of pleading and evidence, 'And especially must there be distinct averments as to the time when the fraud, mistake, concealment, or misrepresentation was discovered, and what the discovery is, so that the court may clearly see whether, by ordinary diligence, the discovery might not have been before made.' Stearns v. Page, 7 How., 819, 829. 'This is necessary to enable the defendant to meet the fraud and the time of its discovery.' Moore v. Greene et al., 19 id. 69, 72. The same rules are laid down in Baubien v. Baubien, 23 id. 190, and in Badger v. Badger, 2 Wall., 95."

This Court then goes on to give many examples illustrating the rule thus emphatically announced, of which the following passage contains a few (141):

> "In Cole v. McGlathry (9 Me. 131), the plaintiff had given the defendant money to pay certain

debts. The defendant falsely affirmed he had paid them, and fraudulently kept the money. It was held that the plaintiff could not recover, because he had at all times the means of discovering the truth by making inquiry of those who should have received the money.

"In McKown v. Whitmore (31 id. 448), the plaintiff handed the defendant money to be deposited for the plaintiff in bank. The defendant told the plaintiff that he had made the deposit. It was held that, if the statement were false and fraudulent, the plaintiff could not recover, because he might at all times have inquired of the bank. In Rouse v. Southard (39 id. 404), the defendant was sued as part owner of a vessel, for repairs, and pleaded the Statute of Limitations. The plaintiff offered evidence that the defendant, when called on for payment, had denied that he was such owner. It was held that, as the ownership might have been ascertained from other sources, the denial was not such a fraudulent concealment as would take the case out of the bar of the Statute.

"Numerous other cases to the same effect might be cited. They all show the light in which courts regard the qualification here in question, of the limitation which would otherwise apply."

See, also, *Consolidated Co. v. Scarborough,* 216 Cal. 698; *Lady Washington Co. v. Wood,* 113 Cal. 482; *Sacramento Lands Co. v. Lindquist* (C.C.A. 9), 39 Fed. (2d) 900; *Bradbury v. Higginson,* 167 Cal. 553.

In the face of this admitted rule, the court below accepted evidence (adduced by Petitioner) showing

what certain officers knew at the very time of the alleged fraud, as being proof that during the many years that followed, the Bank discovered no facts, and was not put on knowledge of any facts, charging it with notice of the allegedly fraudulent transaction.

Plaintiffs in the present case introduced no evidence whatever on the question of when the Bank learned the facts from which the inference of fraud was drawn. Petitioner, however, although not bound to, came forward with evidence to show that at the very time of the alleged fraud, in 1919, many officers and employees of the Bank knew the facts now put forward as constituting the alleged fraud, which facts, indeed, were common knowledge in the Bank at the time, as shown below.

The Trial Court Entirely Misconceived the Question of Laches and the Statute of Limitations.

The trial court, in its opinion, had this to say on the question of Laches and the Statute of Limitations:

> "Admittedly some of the bank officials knew that Herbert Fleishhacker was interested in a deal with the Bardes. * * *
>
> "In this connection it may be observed that while the officers of the Anglo knew of the transaction, it was not at that time known to plaintiff stockholders. * * *
>
> "The evidence shows that discovery [by plaintiff stockholders] of the facts upon which the charges of fraud are based was made in 1933. The

suit was filed on December 5, 1934, within the statutory period. The claim of laches is without merit." (R 190-191, 196)

In its finding the trial court found as follows:

"XIX. It is not true that the plaintiffs or their ancestors or predecessors in interest have been guilty of laches. It is not true that so long a time has elapsed since the matters and things complained of took place that it would be inequitable for this Court to take cognizance thereof.

"XX. It is not true that more than three years before the commencement of this action plaintiffs had knowledge or means of knowledge of the alleged fraudulent acts complained of in the Bill of Complaint, and it is not true that this action is barred by any provisions of the statute of limitations." (R 316)

* * * * * * *

"XI. The facts as to said profits were not known to stockholders of the bank, and none of the plaintiffs herein had any notice or knowledge whatever of the receiving by said Fleishhacker of such profits from the use of funds of the bank as hereinbefore alleged until about the year 1933. Plaintiffs discovered the facts hereinbefore alleged in the following manner:" (R 308)

This finding then continues with a long passage from the complaint, setting out the circumstances of discovery by plaintiff stockholders, in 1933, of the alleged fraud committed in 1919. (R 308-310)

The foregoing quotations from the trial court's opinion and findings demonstrate, we submit, that the trial court held that the Bank had knowledge of the alleged fraud at the time of its commission and (mistakenly believing, as did the plaintiffs, that the plaintiff stockholders and not the bank were the "aggrieved parties") erred in failing to find as requested by Petitioner; that because of the Bank's knowledge, the suit was barred by laches and the Statute of Limitations. (R 259, Nos. XV, XVI)

Treatment in the Court Below of Laches and the Statute of Limitations.

The court below attempted to make the trial court's error of law unimportant, by making a contradictory finding. It discussed Petitioner's evidence showing the extent of the knowledge of certain officers of the Bank at the time of the transaction itself, in 1919, and solely upon the basis of that evidence, concluded as a fact that the plaintiffs had sustained the burden of proving that no officers or responsible employees of the Bank knew, or discovered, or suspected, the facts of the alleged fraud at any time during the following fifteen years.

The foregoing appears plainly on the face of the opinion of the court below. (R 912-914)

If the facts from which the alleged fraud was inferred were discovered or suspected by any responsible bank officer at any time within the twelve-year period intervening between the alleged commission

thereof and December 5, 1931, then this action is barred by laches, by analogy to the three-year statute, this action having been brought December 5, 1934. The evidence that the Bank did not discover, or have reason to suspect, the facts from which the alleged fraud was inferred, at any time during these twelve years, consists exclusively of evidence concerning the knowledge thereof possessed by certain responsible officers of the Bank at the time of the transaction itself, in 1919. Basing its decision on that evidence alone, the court below concluded:

> "We are satisfied that the proof is such as to require a finding that the Bank did not discover the fraud until appellees brought it to light by their investigations. Hence the action is not barred as to the Bank. (R 912) * * *
>
> "It is true that the burden of proving lack of discovery by the Bank rested upon appellees. Earl v. Lofquist, supra; Lady Washington, etc., Co. v. Wood, supra; Consol. Reservoir & P. Co. v. Scarborough, supra. But we think this burden has been discharged." (R 914)

The court below did not mention the defense of laches (which was urged by Petitioner), but addressed itself only to the Statute of Limitations.

In the State Courts, This Action Would Be Governed by the Statute of Limitations.

Sec. 338, subd. 4 of the *California Code of Civil Procedure* provides: [Actions that must be brought within three years]:

> "4. An action for relief on the ground of fraud or mistake. The cause of action in such case not to be deemed to have accrued until the discovery, by the aggrieved party, of the facts constituting the fraud or mistake."

In California, all actions, whether legal or equitable, are governed by one or another of the provisions of the Statute of Limitations: *Piller v. Southern Pacific R. R. Co.,* 52 Cal. 42, 44.

And in California, as elsewhere, a suit in equity may be barred by laches, though brought within the period of the applicable statute: *Boone v. Templeman,* 158 Cal. 290, 299.

It is settled in California that stockholders' suits brought on behalf of the corporation, alleging fraud on the part of an officer or director, are governed by the statute above quoted: *Whitten v. Dabney* (1915) 171 Cal. 621, 628-629; *Pourroy v. Gardner* (1932) 122 Cal. App. 521, 531.

As the court said, in *Earl v. Lofquist* (1933) 135 Cal. App. 373, 376:

> "If the right to maintain the action is barred as to the corporation by the statute of limitations, neither the corporation nor a stockholder in its behalf, irrespective of when he became such, can maintain it. The fact that a stockholder is the nominal plaintiff does not in any manner enlarge the rights and remedies of the action (*Turner v. Markham,* 155 Cal. 562)."

Federal Courts in Equity Cases Follow State Statutes of Limitations by Analogy, Absent Special Circumstances.

This Court has recently summed up the effect in federal courts, sitting in equity, of state Statutes of Limitations: *Russell v. Todd,* .... U. S. ...., 84 L. Ed. (Adv. Op.) 517, 60 S. Ct. 527. As was pointed out in that case, the federal courts, sitting in equity, are not governed by state Statutes of Limitations; but where (as here) the suit is one which, if brought in the state courts, would be governed by a state Statute of Limitations, then the federal courts, in determining whether the suit is barred by laches, will, when consonant with equitable principles, adopt and apply by analogy, the local Statutes of Limitations.

It follows that the present suit is barred by laches, quite apart from the prejudice (discussed below) which Petitioner has suffered because of the long delay. This because the period of the state Statute of Limitations applicable to such suits had not only run, but had run five times over.

And there being no evidence of any kind to excuse the delay by showing the Bank's ignorance of the facts (or that the Bank was dominated by Petitioner at any time during the fifteen-year period), the action necessarily fails. As shown below, moreover, it affirmatively appears, as was found by the trial court, that the facts were known to the Bank in 1919.

The Statute of Limitations Is in Issue.

Although the court below passed upon the issue of the Statute of Limitations, it remarked a doubt whether Petitioner was in a position to urge the bar of the Statute as having run against the Bank, stating that "The pleadings do not specifically frame an issue in respect of the Bank's notice or knowledge of the fraud." (R 912)

Except for this expression by the court below, there has been no intimation, either by counsel or by the trial court, questioning the fact that the Statute of Limitations was in issue; and the Statute has been treated as an issue throughout, both by court and counsel. Since the question is raised by the opinion of the court below, however, we deem it appropriate briefly to discuss the matter.

Perhaps the shortest answer to the suggestion of the court below that the Statute is not in issue, lies in the circumstance that state Statutes of Limitations, as such, are never a direct issue in a suit in equity in the federal courts: The action is barred by delay under the doctrine of laches; and the Statute of Limitations enters only as an analogy, the degree in which it will be regarded as controlling varying with the circumstances detailed in the opinion of this Court in *Russell v. Todd,* supra.

It is settled, therefore, that it is unnecessary to plead the Statute of Limitations in order to invoke laches as a defense. *Waller v. Texas & P. Ry. Co.,*

229 Fed. 87, 92, and cases cited; *Same case* (affirmed) 245 U. S. 398; *Stevenson v. Boyd,* 153 Cal. 630, 636.

As was stated in *Talmash v. Mugleston,* 4 L. J., Ch. (O.S.) 200-01:

> "The rule [of laches] * * * does not result from the statute of limitations. Suppose the rule to be adopted by analogy to the statute, that would not enable the defendant to plead the statute. * * *
>
> "But this Court, like every other, is bound to take notice of every public statute for the purposes of analogy, and of the statute of limitations among the rest. Where a court of equity proceeds by analogy to the statute, it is bound to know the statute, in order to apply the analogy. It is not necessary, therefore, to plead the statute; nor can the rule of the court, [that delay for the statutory period is laches], and the analogy on which it is founded, enable the party to protect himself by such a plea. * * * It can serve no end for him to put in a plea, which only states an act of parliament, to which the court, in applying its rules by analogy to that statute, would be bound to advert."

It is not disputed that laches was properly pleaded. (R 37, 73) We may observe in passing that laches would be in issue even if it had not been pleaded: *Hays v. Seattle,* 251 U. S. 233, 238; *Sullivan v. Portland, etc. R. R. Co.,* 94 U. S. 806, 811; *Richards v. Mackall,* 124 U. S. 183; *Akley v. Bassett,* 189 Cal. 625, 648.

There is no question but what this suit for an accounting of secret profits alleged to have been re-

ceived by an officer of the Bank, is one in equity: 3 Pomeroy, *Equity Jurisprudence* (4th Ed.) Secs. 1090, 1094; *Alexander v. Hillman,* 296 U. S. 222, 239; *Davis v. Pearce,* 30 F. (2d) 85, 88, and cases cited; *Farmers & Merchants' Bank v. Downey,* 53 Cal. 466, 468.

Quite apart from the foregoing, however, the Statute of Limitations, as such, was without doubt an issue in the case. The complaint showed on its face that the alleged cause of action arose fifteen years before the suit was brought. Plaintiffs (failing to realize that the Bank was the aggrieved party) did not allege any excuse for the Bank's delay. Petitioner pleaded the State of Limitations, both in the answer and by motion to dismiss (R 37, 73, 74); and the form of the plea was not questioned by plaintiffs, and in any event was adequate (Rules of Civil Procedure, Form 20, Fourth Defense).

Further references to the Record showing that the Statute was in issue could be multiplied, but we submit, without more, (a) that quite apart from the prejudice suffered by Petitioner because of fifteen years' delay, this suit is barred by laches, by analogy to the Statute of Limitations; and (b) as we presently show, Petitioner has suffered great prejudice from the long delay, and the action is barred for that reason, quite apart from the Statute of Limitations.

The Evidence Shows, the Plaintiffs Admitted, and the Trial Court Found, that the Bank had Notice in 1919.

We have shown that since it was the burden of plaintiffs to allege and prove that failure to sue for fifteen years was not laches because either the Bank did not have knowledge of the alleged fraud or was under Petitioner's domination, it was error of the trial court to fail to find, as requested, that the action was barred, there being no evidence concerning what the Bank knew or discovered between 1919 and 1934, and no evidence of domination.

We now show that the trial court did in fact find that the Bank had notice, in 1919, of the facts from which the court inferred fraud; and that the evidence establishes such notice.

The trial court, in its opinion, stated that,

> "Admittedly some of the Bank officials knew that Herbert Fleishhacker was interested in a deal with the Bardes." (R 190)

and that

> "In this connection it may be observed that while the officers of the Anglo knew of the transaction, it was not at the time known to plaintiff stockholders." (R 191)

This constituted notice to the Bank (*Curtis v. Connly,* 257 U. S. 260, 264). The statement of the trial court that "While the officers of the Anglo knew of the transaction, it was not at the time known to the

plaintiff stockholders" (R 191), is to say (we submit) that if the things that the court finds were known to the Bank officers, were known to the plaintiffs, the latter would be charged with notice.

As noted, the court below held on appeal, (a) that Petitioner's evidence of what was known to the Bank at the time of the transaction in 1919 was not sufficient to show that the Bank then had notice of the alleged fraud, and (b) that this evidence alone was sufficient to sustain plaintiffs' admitted burden of proving that the Bank did not know, or discover, or have grounds to suspect, or have means of ascertaining, the facts from which the alleged fraud was inferred, at any time during the following fifteen years.

As its ground for holding that the Bank was not then (in 1919) charged with notice, the court below said:

> " * * * at most the Bank knew the loans were to be used in a venture in which Fleishhacker was a partner. Burges * * * had been told by Alexander * * * that Fleishhacker was a partner in the steel venture; and nobody considered the matter a secret. But Burges believed, erroneously, that Fleishhacker was a partner in M. Barde & Sons, Inc.; he did not know the details." (R 913)
>
> Mortimer Fleishhacker "knew that the loans were to be used in the new enterprise, but he did not know that they were to be sent East as a deposit on the contract." (R 913) "But he thought that Herbert Fleishhacker 'was to personally put up a large sum of money and the Bardes were to match that sum'; that Herbert Fleishhacker and

the Bardes were to be partners 'and each in a substantial amount' ". (R 913)

"Herbert Fleishhacker stated that he discussed the loans with the * * * Finance Committee * * * explaining that the loans were to be made in connection with a steel deal in which he was to become a partner. It is significant, however, that Fleishhacker did not testify that he ever disclosed the particular terms of his deal with the Bardes. And, if the knowledge of Mortimer Fleishhacker is any criterion (and we think it unlikely that his colleagues on the Finance Committee[1] knew any more than he), it appears that the Bank was actually misled by Herbert Fleishhacker into believing that he, personally, was furnishing half the money for the venture." (R 913-14)

In essence this is to say that the Bank, its Finance Committee, and some of its officers, knew at the time that Petitioner was a partner with the Bardes in a steel venture, that the proceeds of the loans were to be used in that venture, and that no one considered the matter a secret; but that the Bank is not to be charged with notice, because: (a) one of the officers did not know the details and believed Petitioner was a partner in M. Barde & Sons, Inc.; (b) Mortimer Fleishhacker, while he knew the funds were to be used in the new enterprise, did not know they were to be sent East as a deposit on the contract; (c) Petitioner did not disclose the "particular terms" of his deal with the Bardes; and (d) since Mortimer Fleishhacker be-

(1) The two members who died prior to this suit. (R 914)

lieved Petitioner was supplying half the funds (which he was and did), and it was "unlikely" that the other members of the Finance Committee knew any more than he, "it appears that the Bank was actually misled into believing that he, personally, was furnishing half the money for the venture".

The evidence shows that Petitioner in fact did furnish one-half of the capital of the venture, and that the Bank and its officers had knowledge at the time (1919-1920) of the following:

1. That Petitioner was personally interested as a partner in the venture in which the proceeds of the loans were to be used. This was known not only to the members of the Finance Committee, but to other officers, and was a matter of common gossip in the Bank. (R 190, 313, 429, 604-05, 611-12, 624-25, 629, 679-81, 700)

2. That the members of the Executive Committee knew that Petitioner recommended the loans, because his recommendation was made to them. (R 651, 700)

3. That the Bank loans were paid with funds of the Steel Corporation. This was disclosed by the fact that three of the checks of the Steel Corporation in payment, drawn on the Bank, were made out to Petitioner, endorsed by him, delivered by him to the note desk, were cashed and the proceeds applied on the loans. Each check showed on its voucher portion and on its face that one-half the amount thereof was being charged by the corporation to Petitioner personally. (R 388, 614)

4. That Petitioner was a partner with the Bardes and the nature of the partnership. This is shown by a letterhead to that effect taken from the Bank's files at the time of the trial. The letter is dated January 28, 1921, and was written to the Bank. The letterhead lists the partners as follows (R 428):

> "Partners
> J. N. Barde
> H. Fleishhacker
> L. B. Barde
> H. Barde."

It contains the statement in bold printing that Barde Industrial Company was

> "Affiliated with Barde Steel Products Corporation New York City selling 500,000 Tons Steel of U. S. Shipping Board and U. S. Navy";

and that

> "This Company was formed to handle the surplus steel and equipment accumulated by the Government and various industrial corporations throughout the country through cancellation of the war time contracts." (R 429)

5. That Petitioner's stock in the Steel Corporation was issued in the names of nominees, for one of these was an officer and the other an employee of the Bank, one of whom, Klinker, was instructed to include the dividends thereon in Petitioner's income tax return. (R 466)

6. That salary was paid to Petitioner by the Steel Corporation, because the check in payment of the

$50,000 salary was drawn on the Bank, payable to the order of Petitioner, was endorsed by him, and cashed through the Bank. (R 386)

7. The Bank itself was a beneficiary under the agreement dated March 22, 1922, by which the partnership was dissolved, and it must be presumed that it had notice thereof because under such agreement the Bank received certain mortgages. (R 20, 23-24)

8. The Bank therefore knew not only that Petitioner was in the venture in order to receive returns therefrom; it also had ready means of knowing that he received salary and dividends, and an agreed price when he sold out his interest to the Bardes.

9. The facts regarding the Bardes' $175,000 loan at the Central Bank, including Petitioner's guaranty, are shown by the Bank records. On December 22, 1919, the Anglo Bank wrote the Central Bank advising it that on Petitioner's instructions it was debiting the Central National Bank with $175,000, and enclosing the note of M. Barde & Sons for that amount. (R 640, 683) The Bank files contain the letter of the Central National Bank, dated December 23, 1919, acknowledging receipt of the Barde note "together with the guaranty of Herbert Fleishhacker in like amount". The Bank records therefore showed at the time, all of the particulars of the Barde loan at the Central National Bank and Petitioner's guaranty thereof.

10. While the Court below states in its opinion that Mortimer Fleishhacker did not know that any

part of the proceeds of the loans were to be sent East as a deposit on the contract, the Bank records contained a letter of M. Barde & Sons, dated December 16, 1919, carrying a pencil notation by some bank officer that the $250,000 loan proceeds were credited to the Guaranty Trust Company New York. (R 638)

11. The Bank in fact forwarded the $250,000 loan proceeds to Guaranty Trust Company in New York for the account of L. B. Barde. As the Record shows, the same was credited to his account in that Bank on December 23, 1919. (R 532) The Record also shows the Bank knew the disposition of the $325,000 of Anglo Bank loans and the $175,000 Central Bank loans because Klinker, an officer of the Bank, handled the details as to what was done with that $500,000. (R 703)

12. Besides the knowledge which the Bank had of the agreement of dissolution dated March 22, 1922, and that Petitioner sold his interests in the venture to the Bardes and received $200,000 therefor (because it was a beneficiary under that agreement), the Bank also knew all the facts leading up to the making of that agreement and sale, because Klinker, an officer of the Bank, handled the details of the investigation which disclosed the Bardes' abstraction of $200,000 of assets which was the identical amount subsequently received by Petitioner under the agreement of dissolution. (R 690) In fact, Klinker was the person who discovered J. N. Barde's irregularities which led up to the investigation made by him and the subsequent agreement of dissolution. (R 426)

The court below does not know any facts that were not known to the Bank in 1919; yet it has found that a selection from among these same facts are sufficient to sustain an inference that Petitioner committed a fraud and a crime. If they were sufficient for that purpose, were they not much more than sufficient to have put the Bank on inquiry?

The trial court found that there was no express agreement, as alleged, but that there was (in some confused sense) an implied agreement. The court below agreed that there was no express agreement, and "no direct proof" of any agreement, but found by inference that there was an implied agreement, basing its finding to this effect on a view of the facts both different from and contradictory of the view of the facts taken by the trial court.

The point we now make is that in both courts, the finding of a fraudulent agreement rested on acts, not on words, and those acts were known to the Bank and its officers at the time of the transaction.

To say that the Bank's knowledge of the facts did not put it on notice of the inferences which the court below draws therefrom is to say that there is no such thing as a corporation's being put on notice of a fraud, unless some explicit notation of the actual fraud appears in the books and records of the corporation or there is a confession. The application of any such rule would wipe out the protection accorded by the statute of limitations and the doctrine of laches, doctrines which have long been held to be "vital to the

welfare of society and are favored in the law * * * [and] found and approved in all systems of enlightened jurisprudence." (*Wood v. Carpenter,* 101 U. S. 135, 139)

From all the foregoing we submit that if the burden of proof had been upon Petitioner (which it was not) to show affirmatively that the Bank was put upon notice of the alleged fraud fifteen years before the suit was filed, that burden would have been abundantly discharged.

It follows that the suit should have been dismissed on the ground of the laches of the Bank.

Petitioner has Suffered Inequitable Prejudice, and the Suit is Barred by Laches.

Independently of the analogy of the Statute of Limitations, the delay in bringing this suit, in connection with intervening facts and circumstances, has resulted in prejudice to the defendants of such inequitable nature that it is barred by laches. Among the intervening prejudicial facts and circumstances are:

1. The delay of approximately fifteen years between the transactions complained of in December 1919 and the commencement of this suit in December 1934. (R 7, 32)

2. The delay of approximately seventeen years eight months between the transactions complained of and the trial of this suit in August 1937. (R 353)

3. The intervening death of L. B. Barde (R 362), with whom Petitioner made the partnership agreement, thus making it impossible to obtain the testimony of the one person who would have been in a position to corroborate Petitioner's own testimony concerning that agreement.

4. The intervening deaths of Sigmund Stern and J. J. Mack (R 599, 617), who were members of the Bank's Finance Committee at the time of the loans (R 599), and to whom Petitioner disclosed his interest in the venture for which the loans were made (R 678, 679, 700), and who passed on and approved the loans. (R 599, 601, 618)

5. The intervening death of E. R. Alexander (R 611, 617), who was Assistant Vice-President (R 680), Assistant Cashier (R 683, 684), the Executive Officer (R 617) in charge of the Note Department (R 612), and one of the officers who attended Finance Committee meetings. (R 600, 604) Petitioner had disclosed his interest in the venture to Mr. Alexander (R 701), and the latter had discussed the same with Ernest J. Burges. (R 604, 611, 612) In addition, Alexander forwarded the Barde $175,000 note to the Central National Bank of Oakland. (R 683, 684) Mr. Alexander could have given invaluable testimony as to what occurred in the Bank when it made the loans.

6. The intervening death (R 680) of W. E. Wilcox, Vice-President and Cashier. (R 447) Mr. Wilcox, on behalf of the Bank, was connected with certain details of the loans (R 680, 700), and, if living, might

have been able to give definite testimony concerning the same.

7. The intervening deaths of thirteen of the nineteen Directors of the Bank at the time of the loans. (R 599)

8. The removal of the offices of the Bank on two occasions since the transactions in question (R 650), and the possible loss or misplacing of records or correspondence that might have been of value in the defense of this suit.

9. The impossibility, due to lapse of time, of certain and detailed recollection of various facts by several of the witnesses, viz: Samuel Hauser (R 420-4); Etienne Lang (R 547); Mortimer Fleishhacker (R 618-50); and Petitioner.[1] (R 654-703)

Lapse of time in the prosecution of a cause of action which, with intervening circumstances, results in prejudice in the defense of a suit, constitutes laches and operates to bar the action, and such defense, with prejudice shown, may be upheld even though the statutory period of limitation has not elapsed.

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(1) In connection with the question of Petitioner's veracity, it should be noted that in almost every instance when he admitted his lack of definite recollection he could, if he had had any disposition to be untruthful, have given positive and favorable testimony in his own behalf, without contradiction in the record. A dishonest person is seldom without the necessary recollection to fully exculpate himself on all important matters of fact, and even as to minor and immaterial details, and seldom overlooks an opportunity of so doing. Such a person's recollection is usually found to be dim only as to matters of fact that are unfavorable to his cause.

Lapse of time for such a period that it may be reasonably supposed that prejudice has resulted, casts the burden on the plaintiff to show the absence of prejudice. (*Cahill v. Superior Court* (1904) 145 Cal. 42, 47; *Hammond v. Hopkins,* 143 U. S. 224; *Abraham v. Ordway,* 158 U. S. 416, 421)

When, as in the case at bar, there has been great prejudice, and the statutory period of limitation has not only run but has run five times over, a clear case is presented for the application of the doctrine of laches.

In addition to the elements of prejudice already summarized, Petitioner has been greatly prejudiced by the delay, because a claim for interest was allowed which exceeds the amount of the alleged profits. The amount of the judgment is $736,485.57. Of this $348,-125.00 represents the amount of the alleged profits. The remainder, $388,360.57, represents interest thereon. The accumulation of this amount of the interest, because of the long delay in bringing suit, is obviously an element of prejudice. See *Waller v. Texas & Pac. Ry. Co.,* 245 U. S. 398, 412.

POINT III.

THE COURT BELOW HAS SO FAR DEPARTED FROM THE ACCEPTED COURSE OF JUDICIAL PROCEEDINGS AND HAS SO FAR SANCTIONED SUCH DEPARTURES BY THE TRIAL COURT, AS TO CALL FOR EXERCISE OF THIS COURT'S POWER OF SUPERVISION.

The Findings were Prepared by Counsel and Signed Without Change. They are Inconsistent with the Trial Court's Opinion on vital Points and Not Supported by Evidence.

In the present case, the trial judge not only permitted the successful party to prepare the findings, but signed them without any change (R 766); and this notwithstanding that the findings (directed to conform with the opinion (R 197)) change, contradict and are otherwise inconsistent with the view of the facts expressed in the judge's opinion.

Petitioner submitted a detailed request for findings, exceptions to and suggested modifications of plaintiff's proposed findings, and two requests for an opportunity to be heard in connection with settlement of the findings. (R 763-4) All of these were denied (R 765), and plaintiffs' proposed findings were signed as drawn, without any hearing. (R 765-6)

Occasional judicial pronouncements emphasize (what is obvious in any event) that the practice of permitting counsel to prepare the findings of fact and conclusions of law, unless carefully guarded, is dangerous.

In *Process Engineers v. Container Corporation,* 70 F. (2d) 487, 489, the court said:

> "It is urged that the court's findings should be sustained because supported by some evidence. The weakness of this argument lies in the fact that the findings were not made by the court, but are the work of industrious counsel who combined his argument and a partisan and unfair statement of facts into one and called it, 'Findings of Fact.' * * *
>
> "Such so-called findings do not help an appellate court. They reflect the views of counsel who submitted them and detract from the force and effect which are ordinarily given to findings made by the trial judge. When the abuse is aggravated (and the objectionable practice is growing), the assistance to the appellate court, which findings when carefully made by the trial court afford, is lost, and it becomes necessary for us to study the evidence as though no findings had been made by the District Court."

The court, in *Brenger v. Brenger,* 142 Wis. 26 (125 N. W. 109, 113), stated:

> "We are rather forced to the conclusion that the finding belongs to a class, often found troublesome and sometimes fatal to a judgment; those made by judicial sanction of a draft prepared by attorneys for the prevailing party, following some general suggestions from the bench as to the disposition of the case that would be made. That is a very dangerous practice, in the judgment of the writer; a practice which fails to respond to the command of the statute that 'the

judge shall state in his decision separately: (1) The facts found by him: and (2) his conclusions of law thereon.' As said, in effect, on another occasion, 'Such practice, in the judgment of the writer, unless very closely guarded, might well be discontinued altogether.'

" 'Experience shows that counsel, the most able, honorable and conscientious, * * * after the close of a hotly contested case, are not in the frame of mind, ordinarily, best suited to draft the findings which must express the judgment of the court. That is no criticism. It is only an acknowledgment of the natural infirmities of the most perfect of us. All are affected, regardless of ability or purity; the difference is in degree. The making of the findings is purely a judicial function.' Harrigan v. Gilchrist, 121 Wis. 127, 396, 99 N. W. 909.

"Except so far as sanctioned by custom, I know of no warrant for judicial findings to be made up of suggestions as to form and substance, by prevailing counsel, with or without general declarations from the judicial head as to conclusions. The calm sea level, so to speak, of the judicial view is required to respond to the spirit of the Code. It should be seen that these observations are on the writer's personal responsibility, but they are the result of surveys from the viewpoints of a practitioner, a circuit judge and a member of this Court. Doubtless where a judge scans proposed findings eliminating everything not properly a part of such a determination as the statute contemplates, and seeing that all matters of material fact are covered, the preparation of

the paper by counsel proves helpful and is without objection. A practice in that respect so guarded would greatly aid in the administration of justice and is, perhaps, necessary, especially in case of a heavy burden of judicial work.

"If what has already been said does not fully justify the criticisms made of the manner the findings were prepared, the following in connection therewith probably will:"

And in *Nashville, C. & St. L. Ry. Co. v. Price,* 125 Tenn. 646, the court said:

" * * * In accordance with this demand of the trial judge, there was a written findings of fact prepared by the attorney for plaintiffs below. It was signed by the judge and is put into the record as his finding.

"This practice is improper. * * * Such findings are accorded the highest dignity in the appellate courts of Tennessee. They are looked to as embodying a fair statement of all the essential facts in the record, and this Court has said, in Hinton v. Insurance Co., 110 Tenn. 130, 72 S. W. 118, that it will not go outside this finding and examine the record at large for the facts of the case, but will only look to the record to see if the findings of fact are supported by any evidence. There are other cases, familiar to the profession, which further illustrate the weight and force that are here given to these findings of the trial judge.

"The preparation of such a finding, being a matter of so much importance and a high judicial function, cannot properly be intrusted to counsel. Counsel have a natural bias with respect to cases

in which they are engaged that makes it well-nigh impossible for them to fairly and fully present all the facts as the judge would do. We are of opinion, therefore, that his honor was in error in delegating the preparation of the duty imposed upon him by the statute to counsel in the case, and that the finding in this record cannot be looked to by us and treated as a statutory finding of facts by the trial judge. Had exception been taken, the case would have been reversed on this account.

"However, no error being assigned to this action of the trial judge, we have examined the record, as if no special finding had been requested, to see if there is evidence to sustain the judgment below."

It is said in 12 Jour. Am. Jud. Soc., p. 185:

" * * * The *weakest* link in our chain of administering justice is the failure to find the facts as they exist. *Where there is such failure the wrong can never be righted.*" (Emphasis in original)

The following quotation is from an address by Mr. Justice Morgan of the Supreme Court of Idaho:

" * * * it is the practice * * * that the attorney for the party litigant who has won his suit is called upon to prepare the findings for the signature of the trial Judge. * * * Now, you could not find a more biased and prejudiced and badly warped source than that. * * * I have no objection to a trial Judge assigning the duty of preparing the findings to the attorney who wins the case.

But, I would like to have the trial Judge certify that that is what occurred, rather than to leave it to the speculation of the Supreme Court as to whether the trial Judge prepared those findings or not. * * * if the attorney for the respondent makes those findings, and the Trial Judge merely supplies the signature, it ought not to be binding upon the appellate court, because it does not arise from an unbiased source." (Proceedings, Idaho State Bar, 1937, p. 95.)

In the present case, even the form of the findings is strikingly improper. Much of the material in them is simply copied from the complaint, including at several points the words "hereinbefore alleged" or similar expressions. (e.g., R 308, 310)

We now show in parallel columns a few of the many inconsistencies between the trial court's view of the facts as expressed in its opinion, and the view of the facts embodied in the findings drawn by counsel and signed by the court.

The Opinion	*The Findings*
"Herbert Fleishhacker was the president and chief executive officer of the Anglo Bank, receiving an annual salary of $50,000." (R 176)	Herbert Fleishhacker "was president of the bank and chief executive officer thereof in active control of the management of the bank and its operations, and * * * was paid a salary * * * to devote his time and attention to the affairs of the bank, * * *" (R 296)

While this finding appears at first glance to be innocuous, it suggests by implication, (1) that the management of the Bank was under Petitioner's con-

trol and domination, and (2) that under his terms of employment he was not permitted to engage in other activities but was required to devote all of his time and attention to the Bank, both of which implications are contrary to the facts and to the evidence.[1]

The Opinion	*The Findings*
(No such findng).	" * * * said Fleishhacker caused the defendant bank, * * * to loan and advance the sum of $250,000 * * * and caused the defendant bank to advance the further sum of $75,000," (R 298-9)

In its opinion, the court did not find that Petitioner caused the Bank to make the loans in question. All it found was that he "recommended" the loans. (R 178, 189, 190) The finding that Petitioner caused the loans to be made implies either that he was the sole actor for the Bank in the matter, or that the other Bank officers who acted were his puppets.

There is no evidence to sustain a finding that Petitioner "caused" the loans to be made, it being clear that he did not; and the trial court's opinion shows plainly that the judge did not believe any such thing.

The Opinion	*The Findings*
"No showing was made that the loans were ever approved by the board of directors" (R 180)	The "loans * * * were not approved by the board of directors of said bank." (R 300)

(1) There is no implied condition that a bank officer must devote all his time to bank affairs. A corporation officer may engage in outside activities, so long as he acts in good faith. (64 A. L. R. 784)

There is no evidence that these loans were not approved by the Board of Directors.

What the evidence showed was that the Finance Committee had full authority to make loans, and that it made and approved these loans (R 678, 204) The trial court, on the hearing of defendants' motion for leave to introduce in evidence the By-Law of the Bank which shows that the Finance Committee had complete authority in the matter, and also that the Board of Directors in fact approved the loans, said that its statement in the Opinion that no showing had been made that the loans were ever approved by the Board of Directors, constituted purely an incidental remark. (R 751, 752)

The finding in question carries the implication of an irregularity that never occurred, and which the trial court knew never occurred.

The Opinion

"Approximately $1,000,000 would be needed 'to launch the enterprise.' A bidder required $250,000 to qualify his bid. Of the $1,000,000 needed, the sum of $400,000 (including the $250,000 for qualification) would have to be deposited * * * as a guaranty fund, and in addition $500,000 in cash or surety bond for faithful performance. The remaining $100,000 would be for operating capital * * *" (R 176)

The Findings

"* * * defendant Fleishhacker was advised * * * and knew that $250,000 in cash was required to launch the enterprise, * * * [and] that an additional $250,000 would be required * * *" (R 298)

"Said loans and advances aggregating $500,000 constituted the amount of money required to finance the said venture * * *" (R 299)

There is no statement in the findings, as there is in the court's opinion, that the total capital required was $1,000,000, which included the $500,000 supplied by Petitioner. The statement in the findings that only $500,000 was required in the venture, is incorrect, as the opinion and the evidence show.

The Opinion	*The Findings*
(No such finding).	Herbert Fleishhacker "agreed and undertook to finance the said venture, and thereupon * * * caused the defendant bank * * * to loan [the money]. * * * said loans * * * constituted the amount * * * which defendant Fleishhacker had undertaken to procure and make available for the purpose of financing said venture in which he * * * was to have a one-half interest * * *" (R 298-300)

The findings are designed to import a precedent agreement and undertaking by Petitioner, no suggestion of which appears in the court's opinion, or in the evidence. On the contrary, as shown above, the trial court believed, as the evidence showed, that the partnership was formed before Petitioner learned that the Bardes desired to borrow, whether from the Bank or elsewhere.

The Opinion

"* * * upon the recommendation of Fleishhacker, the Anglo Bank loaned the money which made the venture possible. * * * The business was profitable, Fleishhacker's share thereof amounting to about $300,000. Under these circumstances may it not be said that Fleishhacker, president of a national bank, received a thing of value * * * for procuring from his bank a loan to launch the venture?" (R 189-90)

The Findings

"Part of the consideration for the said loans * * * was an agreement between said Bardes and said Fleishhacker that said Fleishhacker should participate in the profits of the enterprise" (R 300)

The reasoning of the trial court on this point is discussed at length below. It must suffice here to say that the trial court plainly believed it to be untrue that there was any factual understanding that Petitioner would receive an interest in the venture if the loans were obtained.

The Opinion

"* * * the Bardes delivered to the Anglo Bank as collateral security * * * Liberty Bonds of the value of $200,000 or more" (R 178); "The loans from the Anglo to [the Bardes] were fully protected." (R 186)

The Findings

The Bardes "delivered to the defendant Fleishhacker or the defendant Bank collateral security consisting of United States Liberty Bonds of the value of $200,000 or thereabouts." (R 300)

The findings import the suggestion that the securities may have been delivered to Petitioner personally; and omit the fact stated in the court's opinion, that the loans were fully protected.

The Opinion	*The Findings*
Barde Steel Products Corporation "subsequently [i. e., after 1919] borrowed on unsecured notes large sums from the Anglo Bank, aggregating at one time $118,000." (R 181)	"Fleishhacker during the year 1920-21-22 caused the defendant Bank * * * to loan other and additional large sums of money to said Barde Steel Products Corporation, such sums aggregating at one time as much as $118,000" (R 308)

There is no evidence whatever as to these loans, except that they were made. There was no evidence that Petitioner had anything to do with them, let alone that he caused them to be made.

The Court Below gave Full Effect to the Findings, Ignoring Discrepancies Between the Findings and the Opinion.

If the opinion of the court below is read in the light of the foregoing, it will be seen that (although the point was argued elaborately and at length) it gave full effect to the most exaggerated discrepancies between the view of the facts entertained by the trial court as expressed in its opinion, on the one hand, and counsel's findings of fact on the other. It will be seen, moreover, that the court below went further, and added to the findings by drawing additional inferences of its own therefrom wherever further findings were necessary to support the decision.

We submit:

(1) That the present case is an extreme example of an undesirable practice concerning the preparation of findings;[1]

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(1) See *Morgan v. United States,* 304 U. S. 1, 19-20.

(2) That such findings, if accepted on appeal, frustrate the appellate process;

(3) That in view of the new Rules of Civil Procedure,[1] findings of fact are now of much greater importance in the administration of justice in the federal courts than heretofore.

The Decision Below Violates Fundamental Principles of the Exigencies of Proof of Fraud.

It has been settled for a long time that fraud is never presumed; that where the evidence or the inferences which it will bear are ambiguous, the presumption favors fair dealing; and that when two inconsistent inferences may equally be drawn, that favoring honesty must be drawn. These principles are particularly important in cases where the charge of fraud is brought forward many years after the event, and after many witnesses have died and the memory of the survivors has been dimmed by time.

In this case it is admitted by both of the inferior courts that there was no express agreement that Petitioner should receive something in exchange for the loans made by the Bank to the Bardes. Everything depends upon inference from conduct. The court below sustains the charge of fraud by drawing inferences from acts which are at least equally consistent with entire honesty. (See Point IV, infra)

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(1) Equity Rule 70½ (now Rule 52(a) Federal Rules of Civil Procedure).

The following authorities are illustrative of the fundamental principle that charges of fraud, particularly stale charges of fraud, are to be examined with great care, and are required to be supported by clear and convincing proof.

> *Stearns v. Page,* 7 How. 818, 829;
> *Halstead v. Grinnan,* 152 U. S. 412, 416;
> *United States v. Arredondo,* 6 Peters, 691, 716;
> *Fidelity & Deposit Co. v. Grand Nat. Bank* (C. C. A., 8) 69 F. (2d) 177, 180-83.

The Opinion in the Court Below Recites the Facts That Appear Suspicious, and Fails to Mention Many Undisputed Facts Tending to Rebut the Charge of Fraud.

On the merits, the opinion of the court below might seem to indicate that the conclusion in favor of fraud is sufficiently supported by evidence to justify its being left undisturbed.

The fact is, however, that this impression is possible only because the opinion of the court below (a) accepts without question the partisan findings prepared by counsel, (b) draws further inferences therefrom when necessary, adds to and contradicts the trial court's view of the facts, and (c) fails to mention numerous undisputed facts and circumstances which show that taking the record as a whole, the evidence is entirely consistent with complete honesty.

We now set out a brief recital of facts, stated chronologically, each of which was either expressly

found to be true by the trial court or is shown by uncontradicted and unquestioned evidence.

We ask the court to contrast this recital with the highly selective statement of the facts in the opinion of the court below.

Facts not mentioned in the opinion of the court below are marked with asterisks.

The Facts.

L. B. Barde and J. N. Barde were brothers living in Portland, Oregon, doing business through their corporation under the name of M. Barde & Sons, Inc., with a net worth of $750,000.* (R 607) Their corporation had done business for a considerable period with the Bank;* and its financial condition was known to the latter's Finance Committee,* its loaning agency, which had authorized an unsecured credit line of $111,000.* (R 451)

L. B. Barde had married a cousin of Petitioner, had introduced himself, and on previous occasions had invited him to join in various ventures, all on a 50-50 basis.* (R 617, 622-3, 654, 655-63, 701-2, 704) For example, in one such proposal, made some months earlier, L. B. Barde wrote Petitioner, "We are prepared to invest One Hundred Thousand Dollars, and you to put in a similar amount."* (R 622)

Petitioner was a man of large means, and engaged in many business enterprises.* (R 621, 654-63, 701-4)

Some time before December 1919, L. B. Barde* proposed that Petitioner become a 50-50 partner with

*Not mentioned in the opinion of the court below.

them in a venture to buy steel from the Shipping Board and resell it. (R 176, 663) The amount of capital consisting of cash or credit was known to be $1,000,000.* (R 176, 364, 664-6, 666, 669, 702-4) The Bardes were to supply half in cash,* and Petitioner was to supply the remaining half in the form of cash, securities, or a bond as required by the Shipping Board* (R 177, 666, 669, 697, 702), and each was to receive a half interest. (R 176, 669, 704) This was agreed to between L. B. Barde and Petitioner, subject to an investigation as to whether the venture was a desirable one. (R 177, 663)

After independent investigation, the parties, about December 1, 1919, agreed to go forward in the venture. (R 177) L. B. Barde reported from the East that $500,000 in cash would be required,* and that the Shipping Board would accept an indemnity bond for $500,000 to secure performance of the contract.* (R 676) This was the half of the capital that Petitioner had agreed to supply as consideration for his half interest.* (R 666, 669, 702)

At this time, as the trial court found in its opinion, it had not been suggested that the Bardes would desire to borrow, whether from the Bank or elsewhere. (R 177, 665, 675) Petitioner testified that he believed the Bardes had the money.* (R 675, 696)

The Bardes thereafter (and only thereafter) asked Petitioner if they could borrow at the Bank. (R 177,

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*Not mentioned in the opinion of the court below.

298, 665, 670, 675, 696, 697) Petitioner presented to the Finance Committee, the loaning agency, Bardes' application for a loan of $250,000 and recommended that it be granted. (R 678, 679, 681, 700) A few days later, he received and presented their application for an additional $75,000. (R 697, 698) Both loans were granted by the Finance Committee. Petitioner did not participate in its action.* (R 599, 601, 618, 636-7, 640, 678-9) The Committee was advised by Petitioner and knew that the funds were to be used in this venture and that he had a personal interest and hoped to make a profit. (R 190, 313, 429, 604-05, 611-12, 620-1, 624-6, 629, 644-6, 652-3, 679, 681, 700) The loans were 6% demand notes of M. Barde and Sons, Inc. endorsed by J. N. Barde and secured by Liberty Bonds of the value of more than $200,000 (R 178, 300, 372-3, 375), and were "fully protected".* (R 186) They were handled in the regular course by the Committee,* which was familiar with the Bardes' credit standing* (R 599-606, 618, 620, 624-5, 629, 634-5, 636-7, 640, 644-5, 649-51, 675, 678-81, 700-1);(1) they were formally recorded* (R 600-6, 618, 636-7); there was no secrecy, and Petitioner's personal interest in the venture, and the fact that the proceeds were used in that venture, were common knowledge in the Bank.* (R 190, 313, 429, 604-5, 611-12, 620-1, 624-6, 629, 644-6, 652-3, 678-81, 700)

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*Not mentioned in the opinion of the court below.

(1) A financial statement dated as of December 23, 1919, of M. Barde & Sons, Inc. showing a net worth of $750,000 was found in the Bank's files. (R 180, 606-7, 639)

Petitioner was unwilling to present to the Bank, the Bardes' request for an additional loan of $175,000* (R 681), but arranged for a loan of this amount to them by the Central National Bank of Oakland, which he personally guaranteed. (R 682)

Of the borrowed money, $250,000 was used as earnest money on the bid to the Shipping Board. On the acceptance of the bid, the Steel Corporation was organized on January 6, 1920 "as an entity for carrying on the enterprise" to use the language of the court below. (R 902)

On January 8, 1920, Petitioner delivered his $500,000 indemnity bond to the Fidelity and Deposit Company of Maryland and thereby obtained its $500,000 bond guaranteeing performance by the Steel Corporation of the Shipping Board contract. (R 685, 687-8) This was done by him pursuant to the terms of the partnership agreement (R 702) as above set forth.* On the same day, the Steel Corporation, in consideration of the payment to it of the $500,000 in cash, and the accepted bid and the contract (of which the $500,000 bond supplied by Petitioner was an express and essential condition (R 86)) to be executed pursuant thereto, authorized the issue to L. B. Barde or his nominees, of 5000 shares of preferred stock and 10,000 shares of common. This stock was issued—one-half to the Bardes and one-half to Petitioner's nominees. In this manner the agreed respective contributions to capital were made and the agreed

*Not mentioned in the opinion of the court below.

respective participating interests were distributed.[1] The Shipping Board executed the contract, secured by $400,000 of the cash, and the $500,000 bond issued upon Petitioner's indemnity. The remaining $100,000 of cash was employed as working capital.

The Steel Corporation paid the Bank loans within four months. Half the amount so paid was charged on its books to the Bardes and half to Petitioner.*

The profits of the Steel Corporation were:*

1920—$ 95,253.28
1921— 140,946.14
1922— 141,807.94

Petitioner received from the Steel Corporation salary amounting to $75,000, and each of the Bardes a like amount, but payment of salaries was discontinued at Petitioner's request.* Petitioner was credited on the books of Barde Industrial Company (a unit of the enterprise) with a dividend of $73,123 on October 1, 1922, and sold his interest in the venture and related ventures to the Bardes for $200,000 on March 22, 1923.

In October 1932 an attorney, employed by one Lang to investigate certain claims against the Bank

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(1) The court below refers to the equal division of the stock, but without mentioning the fact that any other division would have violated the partners' first and only agreement, puts forth as significant, or suspicious, the fact that the stock was issued formally in exchange for the bid and the cash capital.

*Not mentioned in the opinion of the court below.

arising out of oil transactions, called his attention to an item in a detective's report showing that Petitioner had been a partner in the steel venture with the Bardes.* He advised investigating the matter because it might prove to be of assistance in the oil claims.* (R 459) The investigation was made. On October 29, 1934, Lang wrote demanding the Bank bring action against Petitioner. On November 13, 1934, the Bank adopted a resolution declining to bring action,* and this suit was filed December 5th.

In the fifteen years intervening between the date of the loans and the commencement of the suit, two of the four members of the Finance Committee died; E. R. Alexander, the Executive Officer in charge of the note desk, and who attended the Finance Committee meetings, died:* 13 of the 19 directors in office when the loans were made, died:* the Bank had moved its offices twice and records were missing:* and L. B. Barde, with whom Petitioner made the partnership agreement,* died before the trial.*

Interpretation of the Facts.

Having in mind the admitted law, that when these loans were made a national bank officer could personally borrow from the bank:* that at present national banks may lend to partnerships in which their officers own a 50% interest:* and to corporations in which officers own a majority interest:* that it is not a breach of trust for a corporate officer to recommend a transaction in which he is personally interested if

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*Not mentioned in the opinion of the court below.

the transaction is fair to the corporation:* that Petitioner did not act for the Bank in making the loans,* but only recommended them to the Finance Committee, which independently without his participation,* and after investigation* and with knowledge communicated by him of his personal interest in the venture in which they were to be used, authorized them in behalf of the Bank: that they were handled in the regular course:* that there was no secrecy and Petitioner's personal interest in the venture was a matter of common knowledge:* that the loans were sound and desirable and secured by Liberty Bonds and evidenced by notes of a corporation that had previously dealt with the Bank and had been granted unsecured credit up to $111,000;* that the notes were indorsed and guaranteed by J. N. Barde; that the loans were promptly paid—having all these things in mind, it seems inconceivable that many years later a judgment of $736,485 ($852,729.21 as of June 30, 1940) should be rendered against a man whose affairs (by reason thereof) are now in the bankruptcy court, in favor of a Bank which made a good loan, repaid more than 15 years ago, and within four months of the time it was made.

Every single one of the facts we have recited above is established by the evidence; and more, they were admitted as true by plaintiffs and were found to be true in the trial court's opinion. If these facts were recited in the opinion of the court below, no one would

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*Not mentioned in the opinion of the court below.

suggest that they presented a foundation for a judgment that a fraud and a crime had been committed. Can it be that the answer to questions of such importance should depend upon how the facts in an action are arranged and recited?

The trial court found that there was no express agreement for a bonus: it found that there was, in some obscure sense, an implied agreement, and it found the latter, by a process of inference. The court below admits that there is no direct proof to sustain that conclusion. Bearing this in mind, as well as the presumptions in favor of honesty and fair dealing, does not the mere circumstance that the facts can fairly be set down so as to permit, and indeed strongly support, the conclusion that no wrong was committed, compel a finding to that effect, for if an inference of fair dealing can be as readily drawn as an inference of wrongdoing or fraud, the inference of fair dealing must be drawn. And if the facts are such as only to permit the court to say that an inference of fraud "can be drawn", rather than "must be drawn", then the plaintiffs cannot prevail.

The Court below Recast the Whole Factual Setting; and its Decision Rests on a View of the Facts which Contradicts that of the Trial Court.

On the three main issues, the court below affirmed the judgment on the basis of its own inferential findings of fact, which either contradict the trial court's view, or add entirely new inferences to those drawn by the trial court.

Because of the trial court's errors of law, the court below had either to reverse the judgment, or to marshall the whole factual setting anew, and to make fundamental findings and inferences of fact contradictory of the view entertained by the trial court. It chose the latter course:

1. On the merits, the trial court took the position that although admittedly there was no express agreement that Petitioner should receive consideration for the loans or recommending them, there was (in some obscure sense) an implied agreement: the court seemed to believe that since Petitioner recommended the loans, knowing the proceeds were to be used in a venture in which he had an interest, and since that venture (and so, in some sense, the loans) resulted in large profits to Petitioner, it could be said that Petitioner received something of value for the loans or for recommending them. (R 189-90)

The court below took a wholly different view. It contradicted the trial court's finding that the partnership had been formed before the loans were mentioned, and found that the partnership was still only a tentative arrangement at the time the loans were sought. On this basis, it concluded that Petitioner, by continuing with the venture, could be said to have accepted his interest therein in exchange for the loans or for his recommendation of them.

It is indisputable that the trial court had no such idea at all, and indeed that this view is contradicted by the view of the facts entertained by the trial court.

2. Concerning Equity Rule 27 (Rules of Procedure 23(b)), the court supplied a finding, admittedly not made by the trial court, that the Directors of the Bank were guilty of bad faith in refusing to bring the suit; this upon grounds shown by the dissenting opinion to be insufficient.

3. Concerning laches and the Statute of Limitations, the trial court (failing to see that the cause of action was the Bank's and that the Bank was the aggrieved party), held that although "the officers of the Anglo knew of the transaction [at the time it occurred], it was not at that time known to plaintiff stockholders". (R 191) It held on this obviously erroneous ground that the knowledge of the Bank and the delay of fifteen years were irrelevant.

The court below met this difficulty by contradicting the trial court's finding that the Bank's officers knew the facts of the transaction at the time it occurred.

The first of these findings, supplied on appeal, had never been suggested in the case, either by the court below or by counsel. The second is shown by the dissenting opinion to be unsound. As to the third (concerning laches), plaintiffs did argue on the appeal that our evidence of what was known to the Bank in 1919 did not prove that the officers then had notice of the facts complained of; but this contention obviously ignored (as does the reasoning of the court below), the admitted fact that the burden was on plaintiffs to plead and prove lack of discovery by the Bank at any time during the fifteen year period.

The course taken by the court below should be contrasted with the view expressed in the opinion of this Court in *Indiana Farmers' Guide Publishing Co. v. Prairie Farm Publishing Co.*, 293 U. S. 268, 281, where the court said:

> "Respondents had opportunity here to show that, although given on untenable grounds, the judgment below is right and should be affirmed. And, if by the record they could so demonstrate, this court, *if satisfied beyond doubt that it could do so without prejudice to petitioner,* properly might refrain from reversal. * * * Certainly, in the absence of a claim on their part that, conceding the errors exposed by this opinion, the judgment is right, we will not examine the record to discover grounds to sustain it. Cf. *Chicago M. & St. P. Ry. Co. v. Tompkins,* 176 U. S. 167, 179. *Hammond v. Schappi Bus Line,* 275 U. S. 164, 170 et seq. * * *
>
> "The judgment of the Circuit Court of Appeals should be reversed and the case remanded to the District Court with directions that petitioner be granted a new trial." (Emphasis added.)

The two cases cited in the above quotation were equity appeals wherein this Court ordered a new trial because of the insufficiency of the findings.

We submit that for this reason alone, the decree of the trial court should have been reversed.

We submit that the judicial process does not allow the presumption of regularity to be expanded so as to mean that the very decision itself of the trial court is

presumed to be correct, even though the grounds upon which it rests are shown to be unsound, wherefore the judgment should be affirmed if a view of facts can be stated which might have been held to be supported by some evidence if the trial court had found them to be true.

We submit, that the obviously untenable proposition just stated is implicit in the process by which the judgment was affirmed by the court below.

In the next section we show that the view of the facts put forward by the court below is not supported by the record, even if it be given the weight which is properly accorded only to the findings of trial courts.

POINT IV.

ON THE MERITS, NO FRAUD IS SHOWN

Although the trial court's decree against Petitioner was affirmed below, this is not a case within the rule that "concurrent findings of the courts below will be accepted by this Court unless clear error is shown". (*Radio Corp. v. Radio Laboratories*, 293 U. S. 1, 6)

On the contrary, the view of the facts taken in the court below differs radically from that of the trial court, as shown above.

We shall show, moreover, that (as we submit) the facts upon which the lower courts do agree, demonstrate the unsoundness of the judgment.

The Charge Made.

The basis of the suit and the decree is the charge that in 1919, Petitioner received an interest in the

partnership in exchange for aiding the Bardes to obtain loans from the Bank, of which Petitioner was president.

Preliminary Considerations.

Preliminarily the following circumstances should be noted:

1. There is no evidence, nor any attempt to show, that there was an express agreement or understanding between Petitioner and the Bardes that Petitioner should receive this interest or anything else, for the loans. Both courts agree that there was not. (R 187, 906)

2. There is no evidence or attempt to show that Petitioner did anything more toward the granting of the loans by the Bank than to recommend them to the Bank's Finance Committee. That Committee (the Petitioner not participating) approved the loans in the usual course. There is no evidence that Petitioner dominated the Finance Committee or the Board of Directors, or any member of either, or that he put pressure of any kind on them or any of them. Whatever weight his recommendation may have had in fact there is nothing in the evidence concerning it, and no suggestion anywhere in the evidence that it was abnormal or improper in any manner or degree.

The Bardes were Old Customers of the Bank, and their Credit was Excellent.

We come now to the circumstances surrounding the granting of the loans. As we now show, no

imaginable suspicion arises out of the physical fact that these loans were made.

Prior to the transaction here in question, the Barde corporation had done much business with the Bank, having an unsecured line of credit of over $100,000. (R 451) The total of their loans from the Bank during the six months immediately preceding December, 1919, was $138,122.33, which had been reduced to $8,653.45 at the time of the loans complained of. (R 451) Earlier, the Barde corporation had done business with another bank whose president was a member of the Anglo Bank's Finance Committee which passed on the loans. (R 618)

The Bardes were engaged, in Portland, Oregon, in business through their corporation, M. Barde & Sons, Inc., the borrower. (R 176) Their corporation, the borrower, on December 23, 1919, had a net worth of $750,000 (R 607), which fact was known to the Bank at the time it granted the loans. (R 625)

The terms of the loans complained of (6% demand notes) were more favorable than was the general rule in respect of such loans at the time. (R 605, 626-8)

The loans were secured by a pledge of something over $200,000 worth of Liberty Bonds (R 178), and in the language of the trial court, were "fully protected". (R 186)

The making of these loans by the Bank was therefore perfectly natural, and in no way a suspicious circumstance in itself.

The loans being natural, and indeed unusually desirable loans, it was also perfectly natural for Petitioner to recommend them to the Finance Committee.

Although the loans were not to the partnership in which the Petitioner had a half interest, but to Petitioner's partners, they would have been entirely proper if made directly to the partnership, or to Petitioner himself.

Such loans were perfectly lawful, and very common.[1] (R 626-7, 649) Loans to officers of member Banks of the Federal Reserve System were first limited in 1933, the new provision allowing renewals or extensions of existing loans up to 1939, and allowing loans directly to partnerships so long as officers of the Bank do not have more than a half interest. (48 Stat. 182; 49 Stat. 375; 49 Stat. 716; 52 Stat. 223; 53 Stat. 842; 12 U.S.C. §375a)

In 1 *Michie on Banks and Banking,* (Perm. Ed.) p. 145, the rule is stated:

> "In the absence of the statute forbidding loans to officers of the bank, there is no moral or legal turpitude involved in a *bona fide* loan obtained from the bank with the knowledge and consent of the directors."

And see: *Gallin v. National City Bank,* (1934) 273 N. Y. S. 87, 97; *National Bank of Commerce v. Na-*

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(1) See Proceedings of the Subcommittee of the Banking and Currency Committee of the United States Senate, 74th Congress, 1st Session, pp. 79-100.

tional Bank of Missouri, (1878) 30 Fed. Cas. 1121, 1122; *Blair v. First National Bank,* (1877) 3 Fed. Cas. 577, 580; *Witters v. Sowles,* (1887) 31 F. 1; *Briggs v. Spaulding,* (1891) 141 U. S. 132; 3 *Fletcher Cyclopedia of Corporations* (Perm. Ed.), Sec. 955, p. 334.

The undisputed fact is that Petitioner did not keep his relation or interest in this matter a secret. On the contrary, as shown at length above, the essential facts (namely, that Petitioner was a partner in the venture in which the funds were to be used), and indeed most of the details, were common knowledge in the Bank, being known to the officers who testified, and to many others now dead. (R 190, 313, 429, 604, 611, 620, 624, 629, 644, 652, 678, 700)

The Vital Question.

The fact is, then, that the recommendation of these loans by Petitioner (which was his only act of participation as a bank officer in connection with them), and the granting of the loans by the Bank were, in the circumstances, perfectly natural, and furnished the court below no ground for suspicion of wrongdoing.

It is, of course, nevertheless true that if Petitioner in fact received his interest in the partnership in exchange or as consideration for the loans or for his recommendation of the loans, he would be liable in this suit.

The vital question therefore is this: Is there sufficient or any evidence to support an inference of fact that Petitioner did receive an interest in the

partnership for the loans or for his recommendation of the loans to the Bardes?

The Proof, Findings and Admissions are that the Partnership was Formed Before Petitioner Learned that any Loans were Needed or Desired.

The proposition just stated in the heading is shown beyond question. In the first place, Petitioner testified unequivocably that he did not learn of the desire of the Bardes to borrow money, whether from the Bank or elsewhere, until after the partnership had been formed. (R 675) Neither court has questioned Petitioner's credibility as a witness, and indeed, his testimony on this specific question was in terms accepted by the trial court in its opinion which reads in part as follows:

> "After full investigation Herbert Fleishhaker agreed to become a partner in the deal. 'When it came to putting up the money,' testified Herbert Fleishhacker, 'they asked me if they could borrow, if the firm of M. Barde & Sons could borrow some money from the bank.' " (R 177)

The substance of this passage from the court's opinion was carried into the findings: "After having agreed to become an equal partner in said enterprise as aforesaid, the defendant Fleishhacker was advised by the said Bardes" that the sums later borrowed would be required (R 298); and was repeated in the opinion of the court below. (R 901)

The same fact was admitted by counsel for the plaintiff. The following are excerpts from plaintiffs'

briefs in the trial court, which excerpts are in the record. (R 707, ff)

> "Admitted Facts. The following pertinent facts, we [plaintiffs] believe, stand undisputed in the record. * * * Herbert Fleishhacker agreed to enter the deal as an equal partner (that is, on a basis of one-half to Fleishhacker and one-half to the two Bardes) if investigation convinced him the deal would be profitable. * * * After the deal had been investigated and approved and Fleishhacker had agreed to go in as an equal partner, he, Fleishhacker, was advised by the Bardes that they would have to borrow the necessary money. They applied to Herbert Fleishhacker for a loan from the Anglo Bank. Fleishhacker recommended to the finance committee of the bank the approval of loans of $325,000, knowing this money was to be used to launch the venture in which he had a half interest." (R 708-9)
>
> "That Fleishhacker, being informed by his partners that the necessary cash would have to be raised by loans, cooperated in procuring the loans from the bank of which he was president, admits of no question. He did this with full knowledge that the funds coming from the bank would be used in this identical enterprise, for his benefit and his profit." (R 715)

We submit that in these circumstances the conclusion reached below, namely, that Petitioner received his interest in the partnership in exchange for his recommendation of the loans to the Bardes is not supported by the evidence.

We turn now to the processes of reasoning whereby the courts below nevertheless reached a conclusion adverse to Petitioner.

Reasoning of the Trial Court.

Having found that Petitioner did not learn that the Bardes would desire to borrow money (whether from the Bank or elsewhere) until after the partnership agreement had been made (R 177), and that there was no express agreement that Petitioner should receive an interest in the venture for the loans (R 187), the court said:

> "In the Downey case the president of the bank agreed to furnish the money required upon the expressed condition that he should become personally interested to the extent of one-sixth of the profits of the land transaction, while here there was no expressed condition for participation in the profits. This presents the question, Do the facts here justify an inference that a part of the consideration for the loans to the Bardes was an agreement that Fleishhacker should participate in the profits of a deal financed from the funds of the Anglo Bank?" (R 187-8)

The court answered this question as follows:

> " * * * upon the recommendation of Fleishhacker, the Anglo Bank loaned the money which made the venture possible. * * * The business was profitable, Fleishhacker's share thereof amounting to about $300,000. Under these circumstances may it not be said that Fleishhacker, president of a national bank, received a thing of value * * *

for procuring from his bank a loan to launch the venture?" (R 189)

Upon this basis the court concluded "a part of the consideration for the loans" was Petitioner's interest in the partnership. (R 196)

It is, we submit, obvious that the ground for the trial court's decision is thus shown to be, that since the loan by the bank contributed to the success of the venture, and since that loan was made upon the recommendation of Petitioner, those circumstances require the conclusion that Petitioner "received a thing of value * * * for procuring from his Bank a loan to launch the venture."

It is apparent, however, that the trial court's conclusion does not follow from the facts upon which it rests.

The trial court has confused consideration with contributing circumstance.

It is perfectly true (as with every loan to a bank officer or to a partnership or corporation in which he is interested) that the proceeds of the loan contributed to the success of the venture. The vital point is, however, that it is not a wrong—moral, legal or other—for a bank officer to recommend, or for a bank to grant, a loan to persons with whom the bank officer is associated.

We ask this Court to examine the trial court's opinion in full, in order that the Court may have no doubt that the foregoing accurately states the untenable ground of the trial court's decision. (R 175)

Reasoning of the Court below.

The court below paraphrased the findings of the trial court, in part as follows (R 901):

> "Following were the facts as found by the trial court: * * * They [the Bardes] invited Herbert Fleishhacker to join in the proposed enterprise. The Bardes and Fleishhacker conducted independent investigations and decided that the venture would be a profitable one. Thereupon, about December 1, 1919, the Bardes and Fleishhacker agreed to join in the enterprise on the basis that Fleishhacker was to be an equal partner with the two Bardes, namely, a one-half interest to Fleishhacker and one-half to the Bardes.
>
> "After having agreed to become an equal partner, Fleishhacker was advised by the Bardes that $250,000 was required to launch the enterprise, such amount being necessary to qualify the bid, and that, if the bid was successful, an additional $250,000 would be needed."

The court then stated Petitioner's argument that since Petitioner had entered into the venture (and thus received his interest therein) before he learned that the Bardes desired to borrow, it followed that the loans could not have been consideration for that interest. The court disposed of this argument as follows (R 906):

> "The argument is based upon what we regard as an unwarranted interpretation of the findings as a whole, and it is not borne out by the evidence. * * * Prior to the time it became necessary to

> raise the money there had been no definite contract finally determinative of the rights and liabilities of the parties in the venture. All that seems to have been clearly decided was that Fleishhacker was to go in with the Bardes upon a general fifty-fifty basis. The details were uncertain. Necessarily, the entire matter remained at large until the terms of the Shipping Board were finally ascertained and the parties were faced with the specific problem of meeting them."

The trial court's opinion and findings quoted above show plainly that the trial court had no such idea, and as shown, the idea is contradicted by all the relevant evidence.

The court below then says (R 906):

> "It seems plain that Fleishhacker's interest in the venture was proffered him, in substantial measure at any rate, in exchange for anticipated services in the procurement of loans. Fleishhacker must be deemed to have acceded to this condition when his tentative understanding with the Bardes ripened into a definite working contract."

The view of the facts thus adopted by the court below may be summarized as follows:

1. The Bardes offered to enter into an equal partnership in this venture with Petitioner, but concealed the fact that they would want to borrow their contribution to the necessary capital later on.

2. After independent investigation the parties agreed to proceed as equal partners, Petitioner on the one side and the two Bardes on the other.

3. Thereafter when it came to putting up the money, the Bardes informed Petitioner that they desired to borrow part of their contribution to the venture, and asked Petitioner if they could borrow it from the Bank.

4. At this point (the court seems to say), Petitioner could and should have withdrawn. Since the partnership agreement (says the court) was still tentative, because the details were still uncertain, it follows that Petitioner, by recommending the loans to the Bank (instead of refusing to, or withdrawing from the venture), "must be deemed to have acceded" to the theretofore undisclosed intention of the Bardes to proffer Petitioner an interest in the venture "in exchange for anticipated services in the procurement of loans".

There is No Ground for the Conclusion that the Partnership Agreement was Tentative and the Trial Court Found the Contrary.

It is not disputed that prior to any intimation that the Bardes desired to borrow money, the parties had, after independent investigation of the venture, agreed that they would proceed, and that their rights and liabilities should be as follows:

1. The venture would require approximately $1,000,000, in cash or credits (R 176-77, 363-4, 367-8, 663, 666, 669);

2. The Bardes would put up $500,000, in cash if necessary and required (R 665-6, 669);

3. Petitioner would put up $500,000, either in cash, in securities, or in the form of a bond if the Shipping Board would accept a bond (R 669); and

4. Any profits realized would be divided equally, between the Bardes on the one hand and Petitioner on the other. (R 665-6, 669)

The court below does not question these physical facts, but argues that notwithstanding them, the agreement was only tentative, because the details were uncertain.

The contrary is, we submit, clear. In the first place, there is no ground upon which it could be argued that the trial judge found as a fact, or concluded as a matter of law, that the partnership agreement was not a binding agreement. Indeed, as we have shown, the trial court's finding that the partnership agreement was made, is unqualified, and therefore contradicts the conclusion reached by the court below.

The truth is that most oral partnership contracts (which are sustained as sufficiently certain), are far less clear and definite than the agreement here, the making of which is not disputed. See *Carpenter v. Hathaway*, 87 Cal. 434; *Caldwell v. Western Development Co.*, 54 Cal. App. 776; *Watson v. Kellogg*, 129 Cal. App. 592; *Goldsmith v. Sachs*, 17 Fed. 726.

It is, of course, not true that the binding effect of the partnership agreement was impaired by the fact that the manner in which the partners would perform

their obligations was not specified.[1] They seldom are in oral contracts of partnership, and generally cannot be at the time of the contract. (See the cases cited above, particularly *Goldsmith v. Sachs* and *Watson v. Kellogg*.)

We submit that for the court below thus to resort to a strained inference (contrary to the trial court's view of the facts), in order to sustain a charge that a fraud was committed fifteen years before action brought, is not only unfair, but contradicts established principles concerning the exigencies of proof of fraud.

Every essential step in the chain of suspicious circumstances, built up by inference by the court below, is without support in the evidence. There is no suggestion anywhere to support the court's theory that the Bardes planned to obtain the loans by first getting Petitioner into the venture and then disclosing their need to borrow. Even if there were such evidence, it would not affect Petitioner. Unless it is fair to infer from the evidence that when Petitioner was informed that the Bardes desired to borrow, he was thereby led to believe that he had been invited into the venture for the very purpose of getting loans, the fact that he had been, even if it were a fact, would not affect his

(1) This assumes the court below correctly stated that "the details were uncertain." But such is not true, as the only indefiniteness as to manner of performance was the alternative of providing cash of $500,000 or an equivalent thereof in the form of securities or an indemnity (surety company) bond.

good faith. In any event there is no evidence whatever that any such plot was devised, and no intimation that the trial court had any such idea.

Petitioner Contributed Half the Capital.

Both courts below asserted, and treated as a suspicious circumstance, the proposition that (apart from his recommendation of the loans) Petitioner contributed little or nothing to the venture. Thus the trial court said:

> "None of the parties personally contributed any money, but, upon the recommendation of Fleishhacker, the Anglo Bank loaned the money which made the venture possible. * * * Fleishhacker received one-half of the capital stock without paying a dollar of his money for it." (R 189)

Similar language was used by the court below:

> "While Fleishhacker arranged for and guaranteed a faithful performance bond of $500,000 for the Corporation, between him and any possible liability to the surety company lay a cash deposit of at least $400,000. He personally put no money into the enterprise and took small financial risk." (R 908)

It is, we submit, plain that these statements play with words and fail to apply elementary principles of finance. As has been shown, the agreement was that the Bardes should supply half the capital, in cash if necessary, and that Petitioner should supply the remaining half, in cash, securities or a bond as required by the Shipping Board. (R 177, 666, 669, 704) To say

that Petitioner did not put any "money" into the venture is to ignore every-day and universally understood practices. When people invest they do not take currency out of a strong box—they normally supply credit. The California Supreme Court characterized such use of language and disregard of substance as a "paltering with words". (*Grigsby v. Schwarz,* 82 Cal. 278, 281-82)

In this case, all concerned supplied credit. The Bardes obtained their contribution by using their credit to borrow. Petitioner made his contribution by supplying his credit more directly to the venture, i.e., by supplying, not money in the sense of legal tender, but money's worth. The fact that his contribution was identical with actual cash is shown by the agreement itself, under which he was to supply cash, securities, or a bond if the Government would accept a bond. The credit required to provide a surety company indemnity bond of $500,000 as security for a contract involving "the purchase of surplus steel of the value of about $40,000,000" (to use the trial court's words, R 176), is as great as that required to borrow an equal amount.

The risks incurred by Petitioner on the one hand and the Bardes on the other, were identical. The case is of course no different as to risks assumed from what it would be if the Bardes had borrowed from some other lending institution. Their immediate risk was, that should the venture not be profitable, they would have to pay the notes with which they obtained their contribution. Petitioner's immediate risk was

that if the venture should not prove profitable he would become liable to indemnify the surety company on the bond. So long as all or part of the $400,000 cash deposit (made with the Bardes' contribution) was still avaliable, it might be that would be resorted to before recourse was had to the bond.

But the vital point is that the ultimate risks assumed by the parties were identical. The opinions ignore basic principles of partnership law; and the like rules of contribution between co-sureties. It was the majority rule at common law, including California, as it is the rule in California now (Civil Code, Sec. 2412), and elsewhere under the Uniform Partnership Act, that final settlement between partners requires:

1. Crediting each of them with his capital contribution;

2. Crediting or charging each partner with his share of the profits or losses; and

3. Such payments out of the partnership funds, or from one partner to another, as will produce the effect that the net profit or loss realized by each partner is in proportion to his share in the venture.

> "* * * For example, suppose A, B and C have contributed respectively $10,000, $5,000, and $2,000 to the firm's capital of $17,000, and share profits equally. On dissolution, after paying debts there remains $5,000, a capital loss of $12,000. Sharing this equally means a debit to each of $4,000. A would receive $6,000, B would receive

$1,000, and C would pay in $2,000 to meet the deficiency * * * ". (*Crane on Partnership,* p. 281)

See, also, *Sherwood v. Jackson,* 121 Cal. App. 354; 20 *Cal. Jur.* 849 et seq.; *Crane on Partnership,* §§65, 90.

In this connection it is significant that Petitioner's liability for capital contributions was recognized in the manner in which the Bardes' loans at the Bank were paid off. The funds for this purpose were provided by the Steel Corporation, but as each payment was made, half was charged on its books to the Bardes and half to Petitioner. In the same manner Petitioner was charged with one-half of the payments made by the Steel Corporation in discharge of the Central Bank loans to the Bardes. (R 407-10, 432)

Likewise, under the law of contribution between co-sureties, the fact that resort might have first been had to the cash guaranty fund (although not so required by the Shipping Board contract) would not in the least have affected liability to contribute to the Bardes on account thereof.

In every imaginable contingency, therefore, Petitioner's risks were identical with those of the Bardes. If the venture had lost the $500,000 put into it in cash, but no liability had accrued on the bond, then Petitioner would have been obligated to pay to the Bardes the sum of $250,000.

It is perhaps possible to surmise that the risk of the Bardes was more immediate than the risk of Petitioner, i.e., that if the venture had failed the Bardes

would have had to pay their notes prior to the time that Petitioner would have had to respond on his indemnity bond. It is, however, thoroughly unreasonable to conclude on that ground that Petitioner's contribution was substantially less than the contribution made by the Bardes. As a matter of fact, Petitioner's risk continued beyond the time that the immediate risk of the Bardes was discharged. Their notes were paid in four months; Petitioner's bond was outstanding until the contract with the Shipping Board was terminated.

Conclusion on the Merits.

We respectfully submit that the circumstances of the transaction put forward in this case as supporting an inference of fraud furnish no reason even to suspect that fraud was present.

It follows that the charge of fraud (alleged to have been committed fifteen years before suit brought) is unsupported; and that the action of the court below, in finding the evidence sufficient to sustain the charge, contradicts long established rules (a) that fraud is never presumed; (b) that the presumption against fraud approximates in strength that of innocence of crime; and (c) that if two inferences equally susceptible of being drawn from proved facts, one favoring fair dealing and the other favoring corrupt practice, it is the express duty of the court to draw the inference favorable to fair dealing.

The decision opens the door to dangerous and undesirable speculation in stale charges of fraud. See *Conrad v. Nicoll,* 4 Pet. 291, 296-7, 310.

CONCLUSION

The following propositions are, we submit, supported by this petition and brief:

1. The rule announced below emasculates Equity Rule 27 (now Rule of Civil Procedure 23(b)) and the rule of substantive law embodied therein, and opens the federal courts to (a) almost unlimited litigation by stockholders who seek to substitute their judgment concerning corporate policy for that of the Board of Directors, and (b) stockholders' suits brought in bad faith in order to harass the corporation into concessions concerning unrelated matters.

2. The decision opens the federal courts to almost unlimited speculation in stale charges of fraud, by holding that fifteen years of wholly unexplained delay is not laches.

3. The trial court signed, without change, findings prepared by counsel which are inconsistent with the court's own opinion in important particulars, and the court below not only gave full effect to these findings but went further and drew strained inferences therefrom to sustain the decision.

4. The opinions below plainly violate accepted principles concerning the exigencies of proof of fraud, particularly in cases where, as here, the charge is brought forward fifteen years after the event, most of the persons who could have testified concerning the matter being dead.

5. The evidence does not show that Petitioner received a bribe or bonus for procuring a loan of

the Bank's funds, or that he committed any breach of his fiduciary duty to the Bank.

It is submitted that the Writ of Certiorari should be granted, the decree of the court below reversed, and the bill directed to be dismissed.

Respectfully submitted,

HERMAN PHLEGER,
MAURICE E. HARRISON,
Counsel for Petitioner.

JOHN FORD BAECHER,
EVAN HAYNES,
Of Counsel.